



IT IS ORDERED as set forth below:

Date: November 25, 2008

Mary Grace Diehl

**Mary Grace Diehl
U.S. Bankruptcy Court Judge**

**UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION**

In re:	:	BANKRUPTCY CASE NUMBER
	:	08-64071-MGD
CHARLES MICHAEL VAUGHN,	:	
	:	CONSOLIDATED CASE NUMBER
Debtor.	:	08-64060-MGD
	:	
	:	CHAPTER 7

**ORDER DENYING DEBTOR'S CLAIMED EXEMPTION IN CONCEALED
PROPERTY AND DENYING TRUSTEE'S MOTION TO SURCHARGE THE
DEBTOR'S EXEMPTIONS**

This matter came before the Court on Neil C. Gordon's ("Trustee") Objection to Debtor's Claimed Exemptions ("Trustee's Objection"). (Docket No. 39 - Vaughn). Scott Riddle appeared at the hearing as attorney for Charles Michael Vaughn ("Debtor"), but failed to file a written response to the Trustee's motion. The issue before the Court is whether the Court should deny or surcharge Debtor's exemptions pursuant to 11 U.S.C. § 105(a). For the reasons set forth herein, the Trustee's request to deny the debtor's exemptions in the Rolex watch and the boat is **GRANTED**. The Trustee's request to further surcharge the debtor's exemptions for

administrative expenses incurred in recovering estate property is **DENIED**.

I. FINDINGS OF FACT AND PROCEDURAL BACKGROUND

Debtor filed a voluntary Chapter 13 bankruptcy petition (“Debtor’s case”), *pro se*, on March 3, 2008, and Debtor’s company, CM Vaughn, LLC (“CMV”), filed a voluntary Chapter 11 bankruptcy petition on the same date (Case No. 08-64060) (“the CMV case”). On April 18, 2008, the Trustee¹ filed an Emergency Motion to Convert Cases to Chapter 7, to Substantively Consolidate Cases, and for Turnover (“Trustee’s Emergency Motion”). (Docket No. 18 in Debtor’s case and Docket No. 25 in the CMV case).² The Court issued three orders in response to Trustee’s Emergency Motion, two of which are relevant here.³ First, the Court administratively consolidated both cases and converted them to Chapter 7. (Docket No. 41) Trustee was appointed as the Trustee in Debtor’s case. The Court then ordered Debtor and CMV to turnover various items to the Trustee, his attorneys, or his accountants (“the Turnover Order”). (Docket No. 40).

In violation of the Turnover Order, Debtor did not permit the Trustee or his agents onto Debtor’s premises to carry out the Turnover Order. (Trustee’s Objection, ¶ 7). The Trustee and his agents made numerous fruitless attempts to obtain Debtor’s compliance. (Trustee’s

¹ Now the Chapter 7 Trustee in both related cases, Neil C. Gordon was the Chapter 11 Trustee in the CMV case at the time the Emergency Motion was filed.

² Unless stated otherwise, all references to docket numbers hereafter will refer to CMV’s case which became the lead case after consolidation (Docket No. 43 - Vaughn).

³ The Court’s other order, not relevant here, was a denial of the Trustee’s motion for substantive consolidation on an emergency basis. (Docket No. 39). The Court subsequently granted the Trustee’s motion and substantively consolidated the cases on August 6, 2008. (Docket No. 130).

Objection, ¶ 8).

On April 24, 2008, the Trustee filed an emergency motion to compel Debtor to comply with the previous turnover order of the Court (Docket No. 44), which was granted by the Court on April 28, 2008. (Docket No. 45). Debtor again failed to comply with the Court Order and on May 2, 2008, Trustee filed an Emergency Motion for Ex Parte Order Authorizing Trustee to Enter Certain Premises Maintained by Debtor for the Purposes of Retrieving Assets of the Estate (“Motion for Ex Parte Order”). (Docket No. 56). Additionally, Trustee filed an Emergency Motion to Hold Debtors in Contempt of Prior Orders of the Court. (Docket No. 57). The Court granted Trustee’s Motion for Ex Parte Order on May 5, 2005 (Docket No. 60) and found Debtor to be in contempt of court, following a hearing on May 8, 2008. (Docket No. 67).

As of the filing of the Trustee’s Objection,⁴ “the Debtor still has not provided any accounting of investor’s funds nor turned over the documents or his personal laptop computer to assist the Trustee in determining the disposition of such funds.” (Trustee’s Objection, ¶ 18). Debtor concealed from the Trustee both his boat and his Rolex watch, which were not recovered by Trustee until Debtor was held in contempt of court. (Trustee’s Objection, ¶ 24). Trustee and his agents have spent time and incurred administrative expense in searching for and securing estate assets, much of which would not have been necessary if Debtor had complied with the Court’s turnover order. (Trustee’s Objection, ¶ 24).

Debtor has claimed the following exemptions: 1) a \$20,000 homestead exemption in real property located at 565 Trowbrook Road, Atlanta, Georgia 30350; 2) a \$4,700 exemption in

⁴ Trustee timely filed this objection because it was filed within thirty days of the conclusion of the Meeting of the Creditors pursuant to 11 U.S.C. § 341(a).

furniture; 3) a \$300 exemption in clothes; 4) a \$500 exemption in watches; 5) a \$600 exemption in a boat; and 6) a \$3,500 exemption in vehicles. (Docket No. 10, Schedule C - Vaughn).

II. JURISDICTION

This is a core proceeding pursuant to 28 U.S.C. §§ 157(b)(2)(A) and (B). The Court has jurisdiction over this matter under 28 U.S.C. § 1334 and 11 U.S.C. § 105.

III. CONCLUSIONS OF LAW

Trustee has requested that the Court: 1) deny Debtor's exemptions to the extent that they exceed those authorized by O.C.G.A. § 44-13-100; 2) deny Debtor's exemptions in concealed assets;⁵ and 3) surcharge Debtor's remaining assets to compensate the estate for administrative expenses incurred as a result of Debtor's misconduct. Each of these requests are discussed in turn.

A. Denying Debtor's Exemptions That Exceed O.C.G.A. § 44-13-100

The Trustee's Objection contains the general plea that the Court deny Debtor's exemptions to the extent that they exceed those allowed under Georgia Law. Trustee does not make any more detailed argument. However, Debtor's claim of homestead exemption as shown

⁵Trustee also requested that the Court deny Debtor's claimed exemptions in their entirety based on the bad faith of Debtor. The Court does not address the possibility of completely denying exemptions in assets that Debtor did not conceal because both applicable case law and policy fail to support the denial or surcharge of exempt assets solely for the purpose of punishing Debtor for bad faith conduct. *See In re Hamblen*, 354 B.R. 322, 327 (Bankr. N.D. Ga. 2006) (stating that a surcharge is "not punitive" but is necessary for the protection of creditors in preventing the debtors' from "sheltering more assets than permitted by Georgia law"); *Latman v. Burnett*, 366 F.3d 774, 783 (9th Cir. 2004) (stating that a surcharge of debtors' exemptions is "not to punish" the debtors but to "protect the creditors of the bankruptcy estate").

on Schedule C (Docket No 10 - Vaughn) includes a claim of \$20,000.⁶ Georgia exemption law limits an individual's exemption in real or personal property that is used for a residence to \$10,000 except for situations in which title to the property is in one of two spouses who is a debtor, in which case the \$20,000 amount is allowed. Debtor has made no showing that he qualifies for the non-standard amount and therefore his exemption in his residence is limited to \$10,000.

B. Denying Debtor's Exemptions in Concealed Assets

Trustee first requests that this Court deny Debtor's exemptions in assets that Debtor concealed. The Bankruptcy Code permits a debtor, upon the filing of a bankruptcy petition, to exempt from property of the estate certain assets as specified by 11 U.S.C. § 522(d) or state law and non-bankruptcy federal law. 11 U.S.C. § 522(b), (d) (2006). Georgia residents, however, are not allowed to claim exemptions under 11 U.S.C. § 522(d) because Georgia, as authorized by the Bankruptcy Code, has "opt[ed] out" of authorizing its residents to claim the federal exemptions. *In re Hamblen*, 354 B.R. 322, 325 (Bankr. N.D. Ga. 2006); O.C.G.A. § 44-13-100 (2008). Thus, Georgia residents are granted only those exemptions provided by Georgia law.

While a debtor's right to exemptions is significant and has been protected by bankruptcy courts, "it is not absolute." *In re Swanson*, 207 B.R. 76, 81 (D. N.J. 1997); *see also In re Bogan*, 302 B.R. 524, 529 (Bankr. W.D. Pa. 2003); and *In re Doan*, 672 F.2d 831, 833 (11th Cir. 1982) (stating that "concealment of an asset will bar exemption of that asset"). Bankruptcy courts' "authority to deny a claim of exemption in exceptional circumstances is well established." *In re*

⁶The Trustee's objection states that a \$10,000 exemption is claimed but it does not appear that any amendment to this lower number was filed and the Court was not apprised of any agreement by Debtor to the reduced amount.

Stinson, 221 B.R. 726, 728 (Bankr. E.D. Mich. 1998); *see also Doan*, 672 F.2d at 833; *Yonikus*, 996 F.2d 866, 873 (7th Cir. 1993) (holding that Debtor’s exemptions should be denied because Debtor fraudulently concealed the asset); and *Redmond v. Tuttle*, 698 F.2d 414, 417 (10th Cir. 1983) (holding that “[p]roperty fraudulently transferred out of an estate and later recovered by the trustee cannot then be exempted by the debtor”).

Bankruptcy Courts’ authority to deny a debtor’s exemption relies on the general equitable powers found in 11 U.S.C § 105(a), which provides:

The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title. No provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court from, sua sponte, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of the process.

11 U.S.C. § 105(a) (2006).

Although the Code does not explicitly provide that a bankruptcy court may deny a debtor’s exemptions, the 11th Circuit, as well as several other courts, have held that based on § 105(a) a bankruptcy court has the authority to deny an exemption to prevent abuse of the bankruptcy process where the debtor concealed the asset claimed as an exemption. *Doan*, 672 F.2d at 833; *Yonikus*, 996 F.2d at 872. In *Doan*, the Trustee argued that the debtors should be denied leave to amend their exemption schedule to include an exemption of their tax refund from the property of the debtors’ estate. 672 F.2d at 833. The court ultimately concluded that the debtors should be permitted to amend their schedule to include the refund because the court did not believe that the debtors’ had “intentionally or fraudulently” concealed the asset. *Id.* The court agreed, however, that intentional concealment of an asset would “bar exemption of that asset.” *Id.*

In *Yonikus*, a debtor concealed his worker's compensation award, and later claimed an exemption in the award after it was recovered by the trustee. 996 F.2d 866, 868 (7th Cir. 1993). The court held that the debtor should be denied an exemption in his worker's compensation award, reasoning that fraudulently concealing an asset is proper grounds for denial of exemption in that asset. *Id.* at 873.

At least one court has denied a debtor an exemption in an asset where the debtor did not conceal property of the estate, but the conduct of the debtor had the effect of concealment of the property. *Stinson*, 221 B.R. at 732. In *Stinson*, the debtor disclosed and claimed an exemption in a personal injury claim that had not been settled as of the time of her filing for bankruptcy. *Id.* at 728. Subsequently, the debtor settled the claim without involving the court or the Trustee. *Id.* at 727. The court disallowed the debtor's exemption in the personal injury claim. *Id.* at 732. The *Stinson* court based its holding on the fact that the debtor's "subsequent conduct in settling [the] claim created the same result for the estate as if she *had* concealed it in the first instance." *Id.* Thus, "[t]here is no principled basis upon which to distinguish this case from the many in which courts have denied exemption of concealed property." *Id.*

In the present case, Debtor's exemptions in the boat and the Rolex watch should be denied. The majority of cases dealing with denial of exemptions based on concealment of assets involve situations in which the debtor had initially concealed an asset by not listing the asset as property of the estate and or omitting the asset from the list of claimed exemptions. Here, unlike cases such as *Doan* and *Yonikus*, Debtor did list the assets on his initial exemption schedule and is not seeking to amend that schedule. Debtor's conduct in this case, however, like the debtor's conduct in *Stinson*, is tantamount to the initial concealment of the asset. The Trustee made

numerous efforts to get Debtor to comply with the Turnover Order, requiring that the debtor turnover to the Trustee various items including the boat and the Rolex watch.⁷ Debtor testified that he did not know the location of either the boat or the Rolex watch. Only after this Court held Debtor in contempt did Debtor turnover the watch and reveal the location of the boat. For all practical purposes, Debtor's conduct in this case creates the same effect for the estate as if Debtor had concealed the property in the first place. The Trustee had to expend considerable time and effort to uncover the location of these assets to the disadvantage of Debtor's creditors, similar to the time and effort the Trustee would have had to expend to recover assets concealed in the first instance.

Additionally, as in the case of allowing a debtor to claim exemptions in initially concealed assets, allowing Debtor to claim exemptions in assets when he has concealed their location provides no incentive for Debtor to follow the law. To the contrary, it provides an incentive for a debtor to withhold exempt property because there will be no penalty upon his exemptions if later caught. Thus, there is no principled basis upon which to distinguish this case from *In re Doan* and *In re Yonikus*, and Debtor should be denied his claimed exemptions in both the boat and the Rolex watch.

C. Surcharging Debtor's Remaining Exemptions to Cover the Administrative Expenses Resulting from Debtor's Concealment of Assets

Trustee also requests that this Court surcharge Debtor's remaining exemptions to cover the costs of administrative expenses incurred by the estate as a result of Debtor's conduct. The

⁷ The Trustee suggests that Debtor failed to turnover other items, some of which may also have been exempt assets which Debtor concealed, but the record does not clearly reflect that this is the case. (Trustee's Objection, ¶ 6). Accordingly, the Court will not make a determination as to the denial of any assets other than the boat and the Rolex watch.

Court is sympathetic to the fact that the Trustee has incurred expenses far in excess of Debtor's claimed exemptions in recovering assets of the estate. Denying an exemption where a debtor has concealed the location of that asset is consistent with the Bankruptcy Code; however, surcharging a debtor's other exemptions in property that has not in anyway been concealed by the debtor is not.

Only two Circuit Courts have ruled on the question of whether § 105(a) of the Bankruptcy Code permits a court to surcharge a debtor's exempt assets, with the two courts reaching opposite results. *Compare Latman v. Burnett*, 366 F.3d 774, 785 (9th Cir. 2004) with *Scrivner v. Mashburn (In re Scrivner)*, 535 F.3d 1258, 1265 (10th Cir. 2008). *Latman*, and lower courts relying on *Latman*, hold that "[i]n exceptional circumstances, bankruptcy courts have the authority to fashion a remedy [under §105(a)] that allows a trustee to surcharge or offset an exemption." *Hamblen*, 354 B.R. at 325; *see also Latman v. Burdette*, 366 F.3d 774, 786 (9th Cir. 2004); *In re Karl*, 313 B.R. 827, 831 (Bankr. W.D. Mo. 2004). Thus, although the Code does not explicitly provide that a bankruptcy court may surcharge a debtor's exemptions, several courts have held that under § 105(a) they could do so to prevent injustice or an abuse of the bankruptcy system. *See Latman*, 366 F.2d at 786 (holding that "the bankruptcy court may equitably surcharge a debtor's statutory exemptions when reasonably necessary both to protect the integrity of the bankruptcy process and to ensure that a debtor exempts no greater than what is permitted by the exemption scheme of the Bankruptcy Code"); *Hamblen*, 345 B.R. at 327 (holding that "[i]n order to protect the integrity of the bankruptcy process, it [was] necessary to surcharge [a] homestead exemption"). The critical fact in *Latman*, which is not present here, is that the failure to allow the surcharge would have resulted in the debtors having retained exempt

property in excess of the amount allowed under Washington law. Here, the surcharge would serve to reduce Debtor's exemptions below the amounts provided for a "fresh start."

Conversely, and most recently, in *In re Scrivner*, the Tenth Circuit Court of Appeals held that a bankruptcy court did not have the authority to surcharge a debtor's exempt property. 535 F.3d at 1264. In *In re Scrivner*, the debtors owned an interest in the television show "Cheaters" for which they received monthly income. *Id.* at 1261. The debtors failed to surrender any of this post-petition income to the Trustee. *Id.* The Tenth Circuit, reversing the Bankruptcy Appellate Panel, held that the debtors' exempt assets could not be surcharged to satisfy amounts owing the Trustee from the Cheaters income that the debtors failed to surrender. *Id.* at 1264. The court reasoned that "a bankruptcy court may not exercise its 'broad equity powers' under § 105(a) 'in a manner that is inconsistent with the other, more specific, provisions of the [Bankruptcy] Code.'" *Id.* (citing *In re Frieouf*, 938 F.2d 1099, 1103 n.4 (10th Cir. 1991) (quoting *In re Western Real Estate Fund, Inc.*, 922 F.2d 592, 601 (10th Cir. 1990)).

After examining the approaches adopted by the Ninth and Tenth Circuits in resolving the issue of surcharging exempt assets, this Court finds the Tenth Circuit's analysis more persuasive under the facts of this case. Although the equitable powers of the Bankruptcy Court under § 105(a) are broad, they are "not unlimited." *Shapiro v. Saybrook Mfg. Co. (In re Saybrook Mfg. Co.)*, 963 F.2d 1490, 1495 (11th Cir. 1992). Equitable powers of the bankruptcy court "must and can only be exercised within the confines of the Bankruptcy Code." *Norwest Bank of Worthington v. Ahlers*, 485 U.S. 197, 206 (1988).

The Code provides that "[u]nless a party in interest objects, the property claimed as exempt [by the debtor] is exempt." 11 U.S.C. § 522(l) (2006). Additionally "the Code contains a limited

number of exceptions to the rule that exempted property cannot be used to satisfy pre-petition debts or administrative expenses.” *Scrivner*, 535 F.3d at 1264 (citing 11 U.S.C. §§ 522©, (k) (2006) both of which affirmatively provide the general rule that exempt property is not to be charged with administrative expense claims except in specified circumstances). “Like *Scrivner*, the Eleventh Circuit has held that a bankruptcy court’s equitable powers under § 105(a) do not allow it to override a specific provision of the Bankruptcy Code, and do not allow it to grant any more or any less than what the clear language of the Bankruptcy Code would mandate.” *Mazon v. Tardif*, No. 2:07-cv-478-FtM-29, 2008 WL 4234240, at *18 (M.D. Fla. Sept. 9, 2008) (citing *In re Cox*, 338 F.3d 1238, 1243 (11th Cir. 2003)). The enumerated exceptions provided by Congress do not include surcharging exempt assets due to the debtor’s failure to turnover exempt assets or for administrative expenses resulting from that failure. *In re Scrivner*, 535 F.3d at 1264 (citing to 11 U.S.C. §§ 522©, (k) (2006)).

Furthermore, Congress provided “specific remedies for a debtor’s failure to turnover estate property to the trustee.” *Scrivner*, 535 F.3d at 1264. First, a bankruptcy court may deny a debtor a discharge if the debtor transfers, destroys, or conceals property of the estate after the petition is filed “with intent to hinder, delay, or defraud a creditor.” 11 U.S.C. § 727(a)(2).⁸ Secondly, a discharge may be denied if the debtor, while in the case, has refused “to obey any lawful order of the court.” 11 U.S.C. § 727(a)(6)(A) (2006). Finally, a bankruptcy court has the authority to dismiss a Chapter 7 case for “unreasonable delay by the debtor that is prejudicial to creditors.” 11 U.S.C. § 707(a)(1).

Because the Code contains specific circumstances in which a court may use exempted

⁸ Trustee has initiated a § 727 claim against Debtor. (Adv. Pro. No. 08-06444)

property to satisfy pre-petition debts and administrative expenses, and surcharging exemptions for the concealment of property is not such an instance, and because the Code provides remedies for a debtor's misconduct, it would be beyond the scope of this Court's equity powers to grant a surcharge under § 105(a). Thus, the Trustee's request to further surcharge Debtor's exemptions to account for administrative expenses incurred by the estate as a result of Debtor's misconduct in concealing estate property must be denied.

IV. CONCLUSION

The equitable powers of the bankruptcy court under 11 U.S.C. § 105(a) permit the court to craft remedies to prevent abuse of the bankruptcy process. Courts may not, however, take action that is contrary to, or inconsistent with the Bankruptcy Code, to do so would be to exceed the scope of the equitable powers that Congress entrusted to bankruptcy courts.

Accordingly it is

ORDERED that the Trustee's request to deny Debtor's claimed exemptions in both the boat and the Rolex watch is **GRANTED**.

IT IS FURTHER ORDERED that the Trustee's request to surcharge Debtor's additional exemptions is **DENIED**.

The Clerk shall serve a copy of this Order upon Debtor, the Chapter 7 Trustee, and the parties on the attached distribution list.

END OF DOCUMENT

Distribution List

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